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Certain other bonds were subject to buy-back and cancellation in 2006, amounting to €117 million and corresponding to a nominal value of €115 million, detailed as follows:

Nominal value repurchased:	
7.00% EUR due December 2006	€60,485,000
4.375% EUR due February 2009	€54,166,000

The difference between the repurchased amount and the nominal value, corresponding to a charge of €2 million, was included in the financial income (loss) in other financial income (loss), net (see Note 8).

- Repayments
  The balance of the Zero-rate coupon was repaid in June 2006 for a residual nominal amount of €36.4 million.
  The balance of the bonds carrying interest at 7.00% was repaid in December 2006 for a residual nominal amount of €364.9 million.
- Lucent's bonds
  No changes occurred during the month of December 2006, other than the impact of the currency translation adjustment.

Changes in 2005

- Repurchases
  Certain other bonds were subject to buy-back and cancellation in 2005, amounting to €291 million and corresponding to a nominal value of €280 million, detailed as follows:

Nominal value repurchased:	
5.875% EUR due September 2005	€51,627,000
Zero-rate coupon due June 2006	€4,838,724
5.625% EUR due March 2007	€150,925
7.00% EUR due December 2006	€72,603,000
4.375% EUR due February 2009	€150,676,000

The difference between the repurchased amount and the nominal value was included in financial income (loss) in other financial income (loss), net (see Note 8).

- Repayments
  The balance of the bonds carrying interest at 5.875% was repaid in September 2005 for a residual nominal amount of €524.7 million.

Changes in 2004

- Offer to exchange bonds:
  On March 17, 2004, Alcatel-Lucent launched an offer to exchange bonds in a strategy primarily to lengthen its average debt maturity. On March 30, 2004, Alcatel-Lucent announced that bonds with a nominal value of €366 million, coming from Alcatel-Lucent's 7% bond issue of €1.2 billion, due 2006, had been exchanged by the holders for new euro bonds having a nominal value of €412 million, due 2014. The new bonds bear interest at 6.375% *per annum*. Additional bonds having a nominal value of €50 million, which are interchangeable with the new bonds, were also issued. The total nominal value of the new and additional bonds, due 2014, amounts to €462 million. The exchange offer, which closed on April 7, 2004, was recorded in the second quarter 2004. In accordance with IAS 39, such exchange of debt is not considered as an extinguishment of the initial debt and the issuance of new debt, because the borrowing conditions are not substantially different as a result of the exchange transaction. The loss arising on the exchange offer and the related transaction fees are recognized as an adjustment of the carrying amount of the existing debt and are amortized over the remaining life of the adjusted bonds.
- Repurchases and repayments:

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During 2004, certain other bonds were subject to buy-back and cancellation, amounting to €643 million and corresponding to a nominal value of €617 million, detailed as follows:

Repurchased bonds	Nominal value repurchased
5.75% FRF due February 2004	€762,245
5% EUR due October 2004	€22,819,000
5.875% EUR due September 2005	€217,102,000
Zero-rate coupon due June 2006	€111,191,052
5.625% EUR due March 2007	€38,874,495
7% EUR due December 2006	€226,209,000

The difference between the repurchased amount and the nominal value was included in financial income (loss) in other financial income (loss), net (see Note 8).

The other changes for 2004 were the repayment on February 17, 2004 of the residual €183 million on bonds issued by Alcatel-Lucent at a fixed rate of 5.75% in February 1994, and the repayment on October 12, 2004 of the residual €336.4 million in bonds issued at a rate of 5% on October 12, 1999.

(d) Analysis by Maturity Date

(In millions of euros)	2006	2005	2004
Current portion of long-term debt	453	769	910
Short-term debt	708	277	205
Financial debt due within one year	**1,161**	**1,046**	**1,115**
2006	–	–	627
2007	–	364	393
2008	251	104	61
2009	802	878	1,043
2010	10	9	–
2011	924	–	–
2012 and thereafter	3,061	1,397	1,367
Financial debt due after one year	**5,048**	**2,752**	**3,491**
TOTAL	**6,209**	**3,798**	**4,606**

Note: The convertible securities may be retired earlier based on early redemption or buy back options. See Note 24.

(e) Debt Analysis by Rate

(In millions of euros)		2006	
	Amounts	Effective interest rate	Interest rate after hedging
Convertible bonds	2,682	8.34%	8.36%
Other bonds	2,672	6.39%	6.21%
Bank loans and overdrafts and finance lease obligations	556	5.37%	5.13%
Commercial paper	138	3.66%	3.66%
Accrued interest	161	5.84%	5.65%
Financial debt, gross	**6,209**	**7.07%**	**6.97%**

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(f) Debt analysis by type of rate

(In millions of euros)

	2006		2005		2004	
	Before hedging	After hedging	Before hedging	After hedging	Before hedging	After hedging
Total fixed rate debt	6,174	4,155	3,686	1,132	4,468	1,153
Total floating rate debt	35	2,054	112	2,666	138	3,453
TOTAL	**6,209**	**6,209**	**3,798**	**3,798**	**4,606**	**4,606**

(g) Debt Analysis by Currency

(In millions of euros)

	2006		2005		2004	
	Before hedging	After hedging	Before hedging	After hedging	Before hedging	After hedging
Euro	3,000	3,000	3,609	3,609	4,512	4,512
U.S. Dollar	3,171	3,171	141	141	52	52
Other	38	38	48	48	42	42
TOTAL	**6,209**	**6,209**	**3,798**	**3,798**	**4,606**	**4,606**

(h) Fair Value of Debt

The fair value of Alcatel-Lucent's debt is determined for each loan by discounting the future cash flows using a discount rate corresponding to bond yields at the end of the year, adjusted by the Group's credit rate risk. The fair value of debt and bank overdrafts at floating interest rates approximates the net carrying amounts.

At December 31, 2006, the fair value of debt before hedging (and credit spread) amounted to €6,518 million.

The fair value of the financial instruments that hedge the debt is calculated in accordance with the same method, based on the net present value of the future cash flows.

At December 31, 2006, the fair value of the debt after hedging was €6,492 million.

At December 31, 2005, the fair value of debt before hedging (and credit spread) amounted to €4,141 million.

The fair value of the financial instruments that hedge the debt is calculated in accordance with the same method, based on the net present value of the future cash flows.

At December 31, 2005, the fair value of the debt after hedging was €4,033 million.

At December 31, 2004, the fair value of debt before hedging (and credit spread) amounted to €4,926 million.

The fair value of the financial instruments that hedge the debt is calculated in accordance with the same method, based on the net present value of the future cash flows.

At December 31, 2004, the fair value of the debt after hedging was €4,748 million.

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(i) Credit Rating

Credit Ratings of Alcatel–Lucent and Lucent post–Merger

At March 28, 2007, Alcatel–Lucent credit ratings were as follows:

Rating Agency	Long-term Debt	Short-term Debt	Outlook	Last Update	Last update of the outlook
Moody's	Ba2	Not Prime	Stable	December 11, 2006	December 11, 2006
Standard & Poor's	BB–	B	Positive	December 5, 2006	December 5, 2006

At March 28, 2007, Lucent's credit ratings were as follows:

Rating Agency	Long-term Debt	Short-term Debt	Outlook	Last Update	Last update of the outlook
Moody's	Corporate Family Rating withdrawn		n.a	December 11, 2006	n.a
Standard & Poor's	BB–	B–1	Positive	December 5, 2006	December 5, 2006

Moody's: On December 11, 2006, Moody's set Alcatel–Lucent Corporate Family Rating as well as the company senior debt at Ba2 with a Stable outlook. The Not–Prime rating was confirmed for the short–term debt. These ratings have been based on a broad market position, a strong liquidity and a potential for realizing and retaining substantial cost savings balanced by integration and execution challenges.

At the same time, Lucent's Corporate Family Rating was withdrawn assuming that the management of the two entities would be fully integrated over the next several months, which should result in a rapid convergence of the credit risks. Lucent's obligations were upgraded to a range of B3 to Ba3.

Standard & Poor's: On December 5, 2006 Standard & Poor's set the long–term corporate credit rating of Alcatel–Lucent at BB– with a Positive Outlook. The B short–term corporate credit rating was affirmed. These ratings have been based on the fact that the merger had a clear logic and that the combined group would have a larger scale and stronger R&D capabilities. However, this has been mitigated by the fact that the integration process in a very competitive industry would be challenging.

At the same time, Lucent's long–term corporate credit rating was equalized with that of Alcatel–Lucent to BB– with Outlook Positive. Only Lucent's senior unsecured debt ratings remained on Credit Watch with positive implication.

Ratings for Lucent's obligations range from B+ to B–.

Credit Ratings of Alcatel–Lucent and Lucent pre–Merger

Recent history of Alcatel–Lucent's long–term debt credit rating:

Date	Moody's	Date	Standard & Poor's
December 11, 2006	Ba2 Outlook Stable	December 5, 2006	BB– Outlook Positive
April 3, 2006	Ba1 under review	March 24, 2006	BB On credit watch
April 11, 2005	Ba1 Outlook Positive	November 10, 2004	BB Outlook Stable
September 8, 2004	Ba3 Outlook Positive	March 10, 2004	BB– Outlook Stable
May 10, 2004	B1 Outlook Positive	August 11, 2003	B+ Outlook Stable
December 5, 2003	B1 Outlook Stable	October 4, 2002	B+ Outlook Negative
November 20, 2002	B1 Outlook Negative	July 12, 2002	BB+ Outlook Negative

Moody's: On April 3, 2006, Moody's put Alcatel's credit rating under review in view of a possible downgrading of its long–term debt rating (Ba1, positive perspective). This action followed Alcatel's confirmation of discussions with Lucent Technologies regarding a possible merger and was motivated by the strategic and operational changes that would result from such a merger. The ratings themselves (Ba1 and NP) remained unchanged. On September 20, 2006, Moody's communicated that it was expecting to conclude its review of the Group's credit rating on the effective closing date of the above merger. The ratings for Alcatel's debt instruments would be determined later.

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Standard & Poor's: On March 10, 2006, Standard & Poor's changed Alcatel's long-term debt credit rating (BB) outlook from Outlook Stable to Outlook Positive. However, on March 24, 2006, following Alcatel's announcement of its discussions with Lucent Technologies of a possible merger of the two groups, Standard & Poor's placed Alcatel's credit rating on Credit Watch with negative implications, considering that, if the merger went ahead, a downgrading of the long-term debt rating could be envisaged due to the financial structure of the combined entity. The ratings themselves (BB and B) remain unchanged.

Recent History of Lucent's Long-term Debt Credit Rating

Date	Moody's (Corporate Family Rating)	Date	Standard & Poor's
December 11, 2006	Withdrawn	December 5, 2006	BB-[1]
May 16, 2005	B1	March 10, 2004	B
September 10, 2004	B2	October 11, 2002	B-
November 1, 2002	Caa1	September 13, 2002	B
March 22, 2002	B2	March 12, 2002	B+

(1) While the S&P long-term corporate credit rating for Lucent is BB-, its long-term senior debt securities are rated B+.

Rating clauses affecting Alcatel-Lucent and Lucent debt at December 31, 2006

Alcatel-Lucent's short-term debt rating allows a limited access to the commercial paper market.

Alcatel-Lucent's and Lucent's outstanding bonds do not contain clauses that could trigger an accelerated repayment in the event of a lowering of its credit ratings.

(j) Bank Credit Agreements

Alcatel-Lucent Syndicated Bank Credit Facility

On November 10, 2006, the Majority Lenders of the Alcatel-Lucent €1 billion syndicated bank credit facility gave their consent to the waivers to the documentation made necessary to take into account the acquisition with Lucent as well as the proposed disposals to Thales. Under the waiver, a Clean-up period expiring on May 31, 2007 was granted.

On March 15, 2005, Alcatel amended the three-year multi-currency revolving facility that had been put in place on June 21, 2004. Consequently, the maturity date of the facility was lengthened from June 2007 to June 2009, the financial conditions were improved and one of the financial covenants was eliminated. Moreover, Alcatel-Lucent decided to reduce the amount of this revolving facility from €1,300 million to €1,000 million.

The availability of this syndicated credit facility of €1,000 million is not dependent upon Alcatel-Lucent's credit ratings. At December 31, 2006, the credit facility had not been drawn and remained undrawn at the date of approval of the 2006 financial statements by Alcatel-Lucent's Board of Directors. Alcatel-Lucent's ability to draw on this facility is conditioned upon its compliance with a financial covenant linked to the capacity of Alcatel-Lucent to generate sufficient cash to repay its net debt. Alcatel-Lucent has complied with the above covenant every quarter since 2004, when the facility was established.

Lucent Letter of Credit Agreements

Lucent had two primary credit agreements, a letter of credit and reimbursement agreement and an external sharing debt agreement. The first agreement provided for revolving credit loans and letters of credit up to €380 million. The second agreement permitted the extensions of letters of credit. The outstanding obligation under these agreements was €119 million as of December 31, 2006. Both of these agreements were terminated effective March 28, 2007. Outstanding letters of credit previously governed by these agreements remain outstanding under bilateral arrangements with the issuing banks.

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Note 27 – Provisions

(a) Balance at December 31

(in millions of euros)	2006	2005	2004
Provisions for product sales	599	580	662
Provisions for restructuring	413	417	692
Provisions for litigation	403	130	95
Other provisions	916	494	600
TOTAL(1)	**2,331**	**1,621**	**2,049**
(1) Of which: portion expected to be used within one year	1,457	1,024	1,397
portion expected to be used after one year	874	597	652

(b) Change during 2006

(in millions of euros)	December 31, 2005	Appropriation	Utilization	Reversals	Change in consolidated companies	Other	December 31, 2006
Provisions for product sales	580	376	(276)	(181)	105	(5)	599
Provisions for restructuring	417	323	(263)	(80)	34	(18)	413
Provisions for litigation	130	19	(11)	(7)	283	(11)	403
Other provisions	494	119	(54)	(57)	420	(6)	916
TOTAL	**1,621**	**837**	**(604)**	**(325)**	**842**	**(40)**	**2,331**
Effect on the income statement:							
— Income (loss) from operating activities before restructuring, Impairment of intangible assets and capital gain on disposal of consolidated entities		(478)		226			(252)
— restructuring costs		(317)		80			(237)
— other financial income (loss)		(9)		—			(9)
— income taxes		(33)		13			(20)
— income (loss) from discontinued operations and gain/(loss) on disposal of consolidated shares		—		6			6
TOTAL		**(837)**		**325**			**(512)**

At period–end, contingent liabilities exist with regard to ongoing tax disputes. Neither the financial impact nor the timing of any outflows of resources that could result from an unfavorable outcome of these disputes can be estimated at present. Nevertheless, the Group is confident in the outcome of these ongoing disputes.

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(c) Analysis of restructuring provisions

(in millions of euros)	2006	2005	2004
Opening balance	417	692	1,084
Utilization during the period	(263)	(414)	(606)
Charge of the period[1]	243	132	334
Effect of acquisition (disposal) of consolidated subsidiaries	34	(7)	(66)
Cumulative translation adjustments and other changes	(18)	14	(54)
Closing balance	**413**	**417**	**692**

(1) For 2006, €137 million of costs associated with the discontinuance of certain product lines (please refer to Note 3 on the Nortel deal part) for which the Group was committed at year end and €100 million of new restructuring plans or adjustments to previous plans (accounted for in restructuring costs) and €6 million recorded in other financial income (loss) for the amount related to reversing the discount element included in provisions.
For 2005, €89 million of new restructuring plans and adjustments to previous plans accounted for in restructuring and €32 million in discontinued activities. In addition, a finance cost of €11 million was recorded in other financial income (loss) for the amount related to reversing the discount element included in provisions
For 2004, total restructuring costs were €306 million relating to new restructuring plans and adjustments to previous plans. €18 million were booked in discontinued activities. In addition, a finance cost of €10 million was recorded in other financial income (loss) for the amount related to reversing the discount element included in provisions.

(d) Restructuring costs

(in millions of euros)	2006	2005	2004
Social costs	(100)	(101)	(212)
Valuation allowances or write–offs of assets[1]	(470)	11	—
Other monetary costs	(137)	11	(101)
Total restructuring costs	**(707)**	**(79)**	**(313)**

(1) For 2006, mainly related to the discontinuance of some product lines following the merger with Lucent and the acquisition of Nortel's UMTS technologies (refer to Notes 3 and 13).

Note 28 – Market–related exposures

The Group has a centralized treasury management in order to minimize the Group's exposure to market risks, including interest rate risk, foreign exchange risk, and counterparty risk. The Group uses derivative financial instruments to manage and reduce its exposure to fluctuations in interest rates and foreign exchange rates.

Alcatel–Lucent's debt is issued in euros and in US dollars. Interest rate derivatives are used primarily to convert fixed rate debt into floating rate debt.

Firm commercial contracts or other firm commitments are hedged by forward foreign exchange transactions, while commercial bids, which are not firmly committed, are hedged by currency options. The duration of such bids does not usually exceed 18 months.

Because of the diversity of its customers and their diverse geographical locations, management believes that the credit risk relating to customers is limited and that there is no risk of significant credit concentration.

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A — Interest rate risk

Derivative financial instruments held at December 31, 2006 are intended to reduce the cost of debt and to hedge interest rate risk. At December 31, 2006, 2005 and 2004, outstanding interest rate derivatives have the following characteristics:

(a) ***Outstanding interest rate derivatives at December 31***

• Analysis by type and maturity date

(in millions of euros)

	2006					2005		2004	
	Contract notional amounts Maturity date			Total	Market value	Total	Market value	Total	Market value
	Less than one year	1 to 5 years	After 5 years						
Interest rate swaps									
Pay fixed rate	2,342	5,519	81	7,942	(25)	5,609	(10)	4,088	27
Pay floating rate	2,388	7,311	478	10,177	54	8,124	118	7,285	149
Caps									
Buy	1,439	76	—	1,515	3	2,546	12	3,729	13
Sell	1,439	76	—	1,515	(3)	2,419	(12)	2,971	(11)
Floors									
Buy	—	—	—	—	—	—	—	367	2
Sell	—	—	—	—	—	—	—	367	(2)
Forward rate agreements									
Buy	—	—	—	—	—	—	—	—	—
Sell	—	—	—	—	—	—	—	—	—
Options on interest rate swaps U.S.$Libor									
Buy	—	—	—	—	—	212	2	—	—
Sell	—	—	—	—	—	212	(2)	—	—
Total market value	—	—	—	—	**29**		**108**		**178**

• Analysis by accounting category

(in millions of euros)

	Market value		
	2006	2005	2004
Fair value hedges	26	78	146
Cash flow hedge	—	—	—
Instruments not qualifying for hedge accounting	3	30	32
TOTAL	**29**	**108**	**178**

(b) ***Interest rate sensitivity***

Interest rate sensitivity in terms of financial cost

An immediate increase in interest rates of 1%, applied to financial assets and liabilities and related hedging instruments, would decrease interest expense by €5 million for 2006 (€14 million for 2005 and €14 million for 2004).

Interest rate sensitivity in terms of mark-to-market

An increase of 1% in the interest rate curve, applied to financial debt and related hedging instruments, would have a positive impact of €451 million on the market value of the financial debt for 2006 (€53 million for 2005 and €50 million for 2004).

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B — Currency risk

(a)

Outstanding currency derivatives at December 31

• Analysis by type and currency

(in millions of euros)

	2006					2005		2004	
	U.S. dollar	British pound	Other	Total	Market value	Total	Market value	Total	Market value
Buy/Lend foreign currency									
Forward exchange contracts	825	63	716	1,604	(18)	1,785	31	1,722	(37)
Short–term exchange swaps	—	—	—	—	—	589	4	132	(2)
Cross currency swaps	564	128	371	1,063	(19)	—	—	—	—
Currency option contracts:									
— Buy call	677	129	314	1,120	5	590	18	1,406	18
— Sell put	704	75	2,560	3,339	(35)	1 387	(19)	2,653	(72)
TOTAL	**2,770**	**395**	**3,961**	**7,126**	**(67)**	**4,351**	**34**	**5,913**	**(93)**
Sell/Borrow foreign currency									
Forward exchange contracts	2,166	102	376	2,644	30	2,107	(58)	2,924	177
Short–term exchange swaps	892	112	279	1,283	20	1,385	(16)	385	5
Cross currency swaps	—	—	—	—	—	—	—	—	—
Currency option contracts:									
— Sell call	584	4	323	911	(4)	414	(15)	1,455	(17)
— Buy put	1,552	4	2,667	4,223	52	1,774	26	3,032	86
TOTAL	**5,194**	**222**	**3,645**	**9,061**	**98**	**5,680**	**(63)**	**7,796**	**251**
Total market value					**31**		**(29)**		**158**

• Analysis by type and maturity

(in millions of euros)

	Maturity date			
	Less than 1 year	1 to 5 years	After 5 years	Total
Buy/Lend				
Forward exchange contracts	1,604	—	—	1,604
Short–term exchange swaps	1,063	—	—	1,063
Cross currency swaps	—	—	—	—
Currency option contracts:				
— Buy call	1,120	—	—	1,120
— Sell put	2,275	1,064	—	3,339
TOTAL	**6,062**	**1,064**	**—**	**7,126**

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(in millions of euros)

	Maturity date			
	Less than 1 year	1 to 5 years	After 5 years	Total
Sell/Borrow				
Forward exchange contracts	2,643	1	—	2,644
Short–term exchange swaps	1,283	—	—	1,283
Cross currency swaps	—	—	—	—
Currency option contracts:				
— Buy call	911	—	—	911
— Sell put	3,132	1 091	—	4,223
TOTAL	**7,969**	**1,091**	**—**	**9,061**

- **Analysis by accounting category**

(in millions of euros)

	Market value		
	2006	2005	2004
Fair value hedges	18	(37)	113
Cash flow hedge	3	(3)	—
Hedges of net investments	—	—	—
Instruments not qualifying for hedge accounting	10	11	45
TOTAL	**31**	**(29)**	**158**

(b)

Reclassification to income statement of gains or losses on hedges of forecast transactions that were originally recognized in equity

(in millions of euros)

Cash flow hedges accounted for in shareholders' equity at December 31, 2004	**0**
Changes in fair value	2
Reclassification of gains or losses to income statement	–
Cash flow hedges accounted for in shareholders' equity at December 31, 2005	**2**
Changes in fair value	(5)
Reclassification of gains or losses to income statement	(2)
CASH FLOW HEDGES ACCOUNTED FOR IN SHAREHOLDERS' EQUITY AT DECEMBER 31, 2006	**(5)**

Changes in the fair values of cash flow hedges accounted for in shareholders' equity at December 31, 2006 are expected to be reclassified to the income statement for €(5) million in 2007.

C — Stock market risk

Alcatel–Lucent and its subsidiaries are not engaged in speculative trading in the stock markets. Subject to approval by Alcatel–Lucent, subsidiaries may make equity investments in selected companies.

Warrants:

In connection with a Lucent shareholder lawsuit settlement, Lucent issued warrants to purchase 200 million shares of their common stock during December 2004, of which 199 million were outstanding as of December 31, 2006. The warrants have an exercise price of $2.75 per share, gives right to 0.1952 ADSs (American Depositary Shares) Alcatel–Lucent and expire on December 10, 2007.

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Note 29 – Customers' deposits and advances

(in millions of euros)

	2006	2005	2004
Advance payments received on construction contracts	122	704	448
Other deposits and advances received from customers	656	440	525
Total customers' deposits and advances	**778**	**1,144**	**973**
Of which:			
Portion due within one year[(1)]	*636*	*961*	–
Portion due after one year[(1)]	*142*	*183*	–

(1) Data is not available for 2004.

Note 30 – Net cash provided (used) by operating activities before changes in working capital, interest and taxes

(in millions of euros)

	Q4 2006	2006	2005	2004
Net income (loss) attributable to the equity holders of the parent	**(615)**	**(176)**	**930**	**576**
Minority interests	**2**	**45**	**41**	**69**
Adjustments:				
— Depreciation and amortization of tangible and intangible assets	236	631	520	487
Of which impact of capitalized development costs	*77*	*277*	*233*	*183*
— Impairment of intangibles	141	141	–	88
— Changes in pension obligations, net	(40)	(51)	(49)	(38)
— Provisions, impairment losses and fair value changes	804	516	(475)	(534)
— Net (gain) loss on disposal of assets	(62)	(134)	(310)	(137)
— Share in net income (losses) of equity affiliates (net of dividends received)	5	(8)	29	81
— (Income) loss from discontinued operations	(85)	(159)	(110)	(214)
— Finance costs	33	98	93	108
— Share–based payments	17	63	67	58
— Taxes and related reduction of goodwill	(97)	(37)	146	34
Sub–total of adjustments	**952**	**1,060**	**(89)**	**(67)**
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES BEFORE CHANGES IN WORKING CAPITAL, INTEREST AND TAXES	**339**	**929**	**882**	**578**

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Note 31 – Contractual obligations and disclosures related to off balance sheet commitments

(a) Contractual obligations

The following table presents minimum payments that the Group will have to make in the future under contracts and firm commitments as of December 31, 2006. Amounts related to financial debt and finance lease obligations are fully reflected in the consolidated balance sheet.

(in millions of euros)

	Maturity date				
Contractual cash obligations	**Less than 1 year**	**1 to 3 years**	**4 to 5 years**	**After 5 years**	**Total**
Financial debt (excluding finance leases)	1,109	1,053	935	3,060	6,157
Finance lease obligations	52	—	—	—	52
Equity component of convertible bonds	218	—	105	543	866
Sub–total — included in balance sheet	**1,379**	**1,053**	**1,040**	**3,603**	**7,075**
Finance costs on financial debt[(1)]	333	554	438	1,857	3,182
Operating leases	261	401	307	518	1,487
Commitments to purchase fixed assets	40	35			75
Other unconditional purchase obligations[(2)]	503	131	4	—	638
Commitments of discontinued activities[(3)]	9	12	8	12	41
Sub–total — Commitments	**1,146**	**1,133**	**757**	**2,397**	**5,423**

(1) To compute finance costs on financial debt, all put dates have been considered as redemption dates. For debentures with calls but no puts, call dates have not been considered as redemption dates. Further details on put and call dates are given in Note 24. If debentures are not redeemed at the put dates, this will represent an additional finance cost of approximately €1,010 million.
(2) Other unconditional purchase obligations result mainly from obligations under multi–year supply contracts linked to the sale of businesses to third parties.
(3) Commitments of discontinued activities correspond to operating leases for a total amount of €39 million and other unconditional purchase obligations for an amount of €2 million held by entities to be disposed of or contributed to Thales (see Note 3).

(b) Off balance sheet commitments

Off balance sheet commitments of the Group were primarily as follows:

- certain guarantees given to the Group's customers for contract execution (performance bonds, guarantees on advances received issued by financial institutions);
- guarantee relating to the maximum intra–day bank overdraft allowed for Group subsidiaries under the Group's cash pooling agreement with certain banks;
- guarantees given under securitization programs or on sale of receivables (see description below).

Guarantees given in the normal course of the Group's business are presented below.
For guarantees given for contract performance, only those granted by financial institutions are presented below.

(in millions of euros)	**2006**	**2005**	**2004**
Guarantees given on contracts performed by consolidated subsidiaries or by non–consolidated subsidiaries	1,454	2,034	1,742
Discounted notes receivable and other	8	—	5
Other contingent commitments	782	624	793
Commitments of discontinued activities	794	—	—
Sub–total — Contingent commitments	**3,038**	**2,658**	**2,540**
Debt security interests granted and other debt guarantees	60	97	156
Guarantees on cash pooling	579	639	605
TOTAL	**3,677**	**3,394**	**3,301**

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• *Contingent commitments at December 31, 2006*

(in millions of euros)

Contingent commitments	Maturity date				Total
	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years	
Guarantees on Group contracts[1]	906	248	44	66	1,264
Guarantees on third party contracts	137	33	10	10	190
Discounted notes receivable and other	8	—	—	—	8
Other contingent commitments	267	299	40	176	782
Commitments of discontinued activities[2]	413	96	77	208	794
TOTAL	**1,731**	**676**	**171**	**460**	**3,038**
Counter guarantees received	**176**	**14**	**3**	**1**	**167**
Of which related to discontinued activities	27	—	—	—	27
(1) Reflected in balance sheet					147

(2) Commitments of discontinued activities correspond to guarantees on third party contracts for a total amount of €780 million and other contingent commitments for an amount of €14 million held by entities to be disposed of or contributed to Thales (see Note 3).

The amounts reflected in the preceding tables represent the maximum potential amounts of future payments (undiscounted) that the Group could be required to make under current guarantees granted by the Group. These amounts are not reduced by any amounts that may be recovered under recourse provisions in the guarantees or guarantees given by customers for the Group's benefit, which are included in the "counter guarantees received" line.

Commitments related to product warranties, pension and end-of-career indemnities are not included in the preceding table. These commitments are fully reflected in the financial statements. Contingent liabilities arising out of litigation, arbitration or regulatory actions are not included in the preceding table with the exception of those linked to Group construction contracts. For more information concerning contingencies, see Note 34.

Guarantees given on Group construction contracts consist of performance bonds issued by financial institutions to customers and bank guarantees given to secure advance payments received from customers (excluding security interests and restricted cash which are indicated in the table "Guarantees granted on debt, advance payments received, contingencies and security interests granted at December 31, 2006" of this note). Alcatel-Lucent gives guarantees related to advances and payments received from customers, or commits to indemnify the customer, if the contractor does not perform the contract in compliance with the terms of the contract. In the event that, due to occurrences, such as delay in delivery or litigation related to failure in performance on the underlying contracts, it becomes likely that Alcatel-Lucent will become liable for such guarantees, the estimated risk is reserved for on the consolidated balance sheet under the caption "provisions" (see Note 27) or in inventory reserve. The amounts concerned are given in the preceding table in the specific caption "* Reflected in balance sheet".

Commitments related to contracts that have been cancelled or interrupted due to the default or bankruptcy of the customer are included in the above-mentioned "Guarantees on Group contracts" as long as the legal release of the guarantee has not been obtained.

Additionally, most of the performance guarantees given to Group customers are insured. The evaluation of risk related to guarantees takes into account the insurance proceeds that may be received in case of a claim.

Guarantees given on third party construction contracts could contingently require the Group to make payments to the guaranteed party based on a non-consolidated company's failure to perform under an agreement. The fair value of these contingent liabilities, corresponding to the premiums received by the guarantor for issuing the guarantees, was €2 million at December 31, 2006 (€2 million at December 31, 2005 and €3 million at December 31, 2004).

Alcatel-Lucent licenses to its customers software and rights to use intellectual property that might provide the licensees with an indemnification against any liability arising from third-party claims of patent, copyright or trademark infringement. Lucent cannot determine the maximum amount of losses that Lucent could incur under this type of indemnification, because Lucent often may not have enough information about the nature and scope of an infringement claim until it has been submitted.

Alcatel-Lucent indemnifies its directors and certain of its current and former officers for third-party claims alleging certain breaches of their fiduciary duties as directors or officers. Certain costs incurred for providing such indemnification may be recovered under various insurance policies. Lucent is unable to reasonably estimate the maximum amount that could be payable under these arrangements since these exposures are not capped and due to the conditional nature of its obligations and the unique facts and circumstances involved in each agreement. Historically, payments made under these agreements have not had a material effect on its business, financial condition, results of operations or cash flows.

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• Guarantees granted on debt, advance payments received, contingencies and security interests granted at December 31, 2006
(In millions of euros)

Guarantees on borrowings and advance payments received	Maturity date: Less than 1 year	1 to 3 years	4 to 5 years	After 5 years	Total	Total of the balance sheet caption	% of the balance sheet caption
Security interests granted	7	—	—	4	11		
Other guarantees given	29	3	2	15	49		
TOTAL	**36**	**3**	**2**	**19**	**60**		
Net book value of assets given in guarantee:							
— intangible assets	—	—	—	—	—	5,347	—
— tangible assets	7	—	—	—	7	2,026	0.35%
— financial assets	—	—	—	4	4	803	0.50%
— inventories and work in progress	—		—	—	—	2,259	—
TOTAL	**7**	**-**	**-**	**4**	**11**	**10,435**	**0.11%**

• Guarantee on cash pooling

Not included in the preceding table is a guarantee granted to the banks that implement the Group cash pooling. This guarantee covers the risk involved in any debit position that could remain outstanding after daily transfers between Alcatel–Lucent Central Treasury's accounts and the Group subsidiaries' accounts. At December 31, 2006, this guarantee was valued at €579 million (€639 million at December 31, 2005 and €605 million at December 31, 2004).

Specific commitments of former Alcatel

• Sale of carry–back receivable

In May 2002, Alcatel sold to a credit institution a carry–back receivable with a face value of €200 million resulting from Alcatel–Lucent's decision to carry back 2001 tax losses. This receivable is kept in the consolidated balance sheet with the contra entry in financial debt because of the Group's ability to recover this receivable before its maturity date.

Alcatel–Lucent is required to indemnify the purchaser in case of any error or inaccuracy concerning the amount or nature of the receivable sold. The sale will be retroactively cancelled in the event of a modification to the law or regulations that substantially changes the rights attached to the receivable sold.

• Securitization of customer receivables

In December 2003, Alcatel entered into a securitization program for the sale of customer receivables without recourse. Eligible receivables are sold to a special purpose vehicle, which benefits from a subordinated financing from the Group representing an over–collateralization determined on the basis of the portfolio of receivables sold. This special purpose vehicle is fully consolidated in accordance with SIC 12.. This program was temporarily frozen in December 2006, and the balance of receivables sold at December 2006 was therefore zero. Receivables sold in previous years that amounted to €61 million at December 31, 2005 and €82 million at December 31, 2004 were maintained in the consolidated balance sheet. The December 2006 freeze has therefore no impact on the Group's balance sheet.

At December 31, 2006, the maximum amount of receivables that could be sold amounted to €150 million (€150 million at December 31, 2005 and €150 million at December 31, 2004), representing a credit line available to the Group. This amount can be increased to €250 million. The purpose of this securitization program is to optimize the management and recovery of receivables in addition to providing extra financing.

Specific commitments of Lucent

Lucent's Separation Agreements

Lucent is party to various agreements that were entered into in connection with the separation of Lucent and former affiliates, including AT&T, Avaya, Agere Systems and NCR Corporation. Pursuant to these agreements, Lucent and the former affiliates have agreed to allocate certain liabilities related to each other's business, and have agreed to share liabilities based on certain allocations and thresholds. Lucent is not aware of any material liabilities to its former affiliates as a result of the separation agreements that are not otherwise reflected in its unaudited consolidated financial statements. Nevertheless, it is possible that potential liabilities for which the former affiliates bear primary responsibility may lead to contributions by Lucent.

Lucent's Other Commitments

Contract Manufacturers

Lucent has outsourced most of its manufacturing operations to electronic manufacturing service (EMS) providers. Two EMS providers supply most of Lucent designed wireless and wireline products. Celestica has the exclusive right to manufacture and provide most of Lucent's existing wireless products. Solectron Corporation consolidates the outsourced manufacturing of Lucent's portfolio of wireline products. The agreements with Celestica and Solectron are for a minimum of three years, with no right to terminate for convenience. Lucent is generally not committed to unconditional purchase obligations in these contract–manufacturing relationships. However, there is exposure to short–term purchase commitments when they occur within the contract manufacturers' lead–time for specific products or raw materials. These commitments were $309 million as of December 31, 2006. Sudden and significant changes in forecasted demand requirements within the lead–time of those products or raw materials could adversely affect Lucent's results of operations and cash flows.

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Lucent's guarantees and Indemnification Agreements

Lucent divested certain businesses and assets through sales to third–party purchasers and spin–offs to its common shareowners. In connection with these transactions, certain direct or indirect indemnifications are provided to the buyers or other third parties doing business with the divested entities. These indemnifications include secondary liability for certain leases of real property and equipment assigned to the divested entity and certain specific indemnifications for certain legal and environmental contingencies, as well as vendor supply commitments. The time durations of such indemnifications vary but are standard for transactions of this nature.

Lucent remains secondarily liable for approximately $162 million of lease obligations as of December 31, 2006, that were assigned to Avaya, Agere and purchasers of other businesses that were divested. The remaining terms of these assigned leases and the corresponding guarantees range from one month to 14 years. The primary obligor under assigned leases may terminate or restructure the lease obligation before its original maturity and thereby relieve Lucent of its secondary liability. Lucent generally has the right to receive indemnity or reimbursement from the assignees and have not reserved for losses on this form of guarantee.

Lucent is party to a tax–sharing agreement to indemnify AT&T and is liable for tax adjustments that are attributable to its lines of business, as well as a portion of certain other shared tax adjustments during the years prior to its separation from AT&T. Lucent has similar agreements with Avaya and Agere. Certain tax adjustments have been proposed or assessed subject to these tax–sharing agreements. The outcome of these other matters is not expected to have a material adverse effect on Lucent's consolidated results of operations, consolidated financial position or near–term liquidity.

Note 32 – Related party transactions

To the Group's knowledge, the only shareholders holding more than 5% of the parent company's share capital are Brandes Investment Partners LP and Fidelity.

Transactions with related parties (as defined by IAS 24 "Related Party Disclosures") during 2006, 2005 and 2004 were as below:

Related parties are mainly:

- shareholders of Alcatel–Lucent SA,
- share of the transactions of jointly controlled entities (consolidated using proportionate consolidation) related to other venturers,
- investments in associates (accounts for using equity method),
- non consolidated entities,
- key management personnel.

(in millions of euros)	**2006**	**2005**	**2004**
Revenues			
Non–consolidated affiliates	39	44	42
— Joint ventures	—	—	—
— Equity affiliates	27	9	11
Cost of sales			
— Non–consolidated affiliates	(41)	(48)	(67)
— Joint ventures	(128)	(145)	(120)
— Equity affiliates	(38)	(23)	(4)
Research and development costs			
— Non–consolidated affiliates	(7)	(7)	(5)
— Joint ventures	(17)	(36)	(41)
— Equity affiliates	(4)	(3)	—

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Outstanding balances arising from related party transactions at December 31, 2006, 2005 and 2004 were as follows:

(in millions of euros)	2006	2005	2004
Other assets			
— Non–consolidated affiliates	31	21	41
— Joint ventures	2	30	35
— Equity affiliates	24	29	14
— Valuation allowances	(12)	(20)	(6)
Other liabilities			
— Non–consolidated affiliates	(10)	(22)	(20)
— Joint ventures	(17)	(50)	(18)
— Equity affiliates	(23)	(32)	(15)
Cash (financial debt), net			
— Non–consolidated affiliates	(1)	—	(11)
— Joint ventures	(60)	(11)	15
— Equity affiliates	(30)	(38)	(31)

Members of the Board of Directors and members of the Group's executive committee are those present during the year and listed in the Corporate Governance section of the Annual Report. In 2006, 2005 and 2004, compensation, benefits and social security contributions attributable to members of the Board of Directors and to the executive committee members ("Key management personnel") were as follows:

Recorded expense in respect of compensation and related benefits attributable to Key management personnel during the year

(in millions of euros)	2006	2005	2004
Short–term benefits			
Fixed remuneration	7	7	7
Variable remuneration[(1)]	5	7	4
Directors' fees	1	1	1
Employer's social security contributions	5	4	4
Termination benefits and retirement indemnities	7	5	—
Other benefits			
Post–employment benefits	6	5	4
Share–based payments (stock option plans)	4	5	5
TOTAL	**35**	**34**	**25**

(1) Variable remuneration includes retention bonuses.

Note 33 – Payroll and staff training rights

(in millions of euros)	2006	2005	2004
Wages and salaries (including social security/pension costs)	3,392	3,702	3,740

The law of May 4, 2004 in France provides French company employees with the right to receive individual training of at least 20 hours per year that can be accumulated over six years. Rights related to terminated or dismissed employees exercised during the notice period and rights exercised by employees considered as not adapted to the needs of their employer or not professional in nature, are assimilated to short and long–term employee benefits as defined in IAS 19 and have been provided for accordingly. All other rights are accounted for as incurred, as the employer expects to receive an amount of economic benefits from the training to be taken, greater than the costs to be incurred to settle the present obligation.

Accumulated individual staff training rights were 652,811 hours at December 31, 2006 (601,179 hours at December 31, 2005 and 312,400 hours at December 31, 2004). Rights exercised so far are not material.

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Note 34 – Contingencies

In addition to legal proceedings incidental to the conduct of its business (including employment–related collective actions in France and the U.S.) which management believes are adequately reserved against in the financial statements or will not result in any significant costs to the Group, Alcatel–Lucent is involved in the following legal proceedings:

France Telecom

Since 1993, a legal investigation has been ongoing concerning "overbillings" which are alleged to have been committed in Alcatel CIT to the detriment of its principal client, France Telecom, based on an audit of production costs conducted in 1989 in the transmission division, and in 1992 in the switching division. Two settlement agreements were entered into with France Telecom, one in 1993 in relation to the transmission division, and the other in May 2004 in relation to the switching activity: in the latter it was recognized that the parties' dispute on pricing did not involve fraud by Alcatel CIT. In April 1999, Alcatel learned that the criminal investigation had been extended to determine whether corporate funds of Alcatel CIT and Alcatel had been misused. As a consequence, both Alcatel CIT and Alcatel filed civil complaints to preserve their rights with respect to this investigation.

The investigating magistrate has recently closed his judicial inquiry. Pursuant to his ruling of May 16, 2006, an ex–employee of Alcatel CIT and two of his supervisors, each of whom left the Group several years ago, will be brought before the criminal court of Evry for the overbilling that allegedly occurred in the transmission division. On the other hand, the judge ruled that there are no grounds for the prosecution of all the other suspects (three in the transmission division and seven in the switching division), which include Alcatel CIT. Alcatel CIT remains a party to the procedure as a plaintiff pursuant to its civil complaint. With respect to the procedure regarding a potential misappropriation of corporate funds at Alcatel CIT and Alcatel, the judge issued an order to dismiss on November 16, 2006, and this case is now over since neither the Prosecutor nor any party appealed such order.

Class A and Class O shareholders

Several purported class action lawsuits have been filed since May 2002 against Alcatel–Lucent and certain of its officers and directors challenging the accuracy of certain public disclosures that were made in the prospectus for the initial public offering of Alcatel Class O shares and in other public statements regarding market demand for the former Optronics division's products.

The lawsuits purport to be brought on behalf of persons who (i) acquired Alcatel Class O shares in or pursuant to the initial public offering of the American Depositary Shares ("ADS") conducted by Alcatel in October 2000, (ii) purchased Alcatel Class A and Class O shares in the form of ADSs between October 20, 2000 and May 29, 2001 and (iii) purchased Alcatel Class A shares in the form of ADSs between May 1, 2000 and May 29, 2001. The amount of damages sought by these lawsuits has not yet been specified.

The actions have been consolidated in the United States District Court, Southern District of New York. Alcatel filed a motion to dismiss this action on January 31, 2003 and a decision on the motion was rendered on March 4, 2005. The judge rejected a certain number of the plaintiffs' demands with prejudice. He also rejected all the remaining claims under the federal securities laws for lack of specificity in the pleadings, but with leave to file a further amended complaint. This was filed, and fully briefed as of August 5, 2005. The parties are waiting for the judge's decision.

Costa Rica

Beginning in early October 2004, Alcatel learned that investigations had been launched in Costa Rica by the Costa Rican Prosecutor's and the National Congress, regarding payments alleged to have been made by consultants on behalf of Alcatel CIT, a French subsidiary ("CIT ") or other Alcatel subsidiaries to various public officials in Costa Rica, two political parties in Costa Rica and representatives of ICE, the state–owned telephone company, in connection with the procurement by CIT of several contracts for network equipment and services from ICE. Upon learning of these allegations, Alcatel immediately commenced an investigation into this matter, which is ongoing.

In Costa Rica and other countries, Alcatel–Lucent's subsidiaries retain consultants to assist with local operations and contracts. Alcatel–Lucent's contracts with persons through whom Alcatel–Lucent deals locally strictly prohibit the provision of any pecuniary or other advantage in contravention of applicable laws. In addition, Alcatel–Lucent has a strict Statement of Business Principles (a copy of which is available on its web site, www.Alcatel–Lucent.com, under the heading "Business Ethics and Compliance") that imposes the highest standards of legal and ethical conduct on its employees. Alcatel–Lucent rigorously enforces this Statement of Business Principles across the entire company and, when violations occur, Alcatel–Lucent takes prompt and appropriate action against the persons involved.

Alcatel terminated the employment of the then president of Alcatel de Costa Rica in October 2004 and of a vice president Latin America of CIT. CIT is also pursuing criminal actions in France against the latter and in Costa Rica against these two ex–employees and certain local consultants, based on CIT's suspicion of their complicity in an improper payment scheme and misappropriation of funds. The contracts with the local consultants were limited to the specific projects involved and are no longer in effect or have been terminated, and any payments due under those contracts have been suspended.

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Alcatel contacted the United States Securities and Exchange Commission and the United States Department of Justice and informed them that Alcatel–Lucent would cooperate fully in any inquiry or investigation into these matters. The SEC and the Department of Justice are conducting an investigation into possible violations of the Foreign Corrupt Practices Act (FCPA) and the Federal Securities Laws. If the Department of Justice or the SEC determines that violations of law have occurred, it could seek civil or, in the case of the Department of Justice, criminal sanctions, including monetary penalties against Alcatel–Lucent.

In connection with these allegations, on December 19, 2006, the Department of Justice indicted the former CIT employee on charges of violations of the FCPA, money laundering, and conspiracy. On March 20, 2007, a grand jury returned a superseding indictment against the same former employee and a second former employee, based on the same allegations contained in the previous indictment. That case is currently set for trial on July 9, 2007, in the Southern District of Florida.

Neither the Department of Justice nor the SEC has informed Alcatel–Lucent what action, if any, they will take against Alcatel–Lucent and its subsidiaries.

Several investigations have been launched in Costa Rica concerning this matter by both the Costa Rican Prosecutor's Office and ICE. On November 25, 2004, the Costa Rican Attorney General's Office commenced a civil lawsuit against CIT to seek compensation for the pecuniary damage caused by the alleged payments described above to the people and the Treasury of Costa Rica, and for the loss of prestige suffered by the Nation of Costa Rica. On February 1, 2005, ICE commenced a lawsuit against CIT to seek compensation for the pecuniary damage caused by the alleged payments described above to ICE and its customers, and for the harm to the reputation of ICE resulting from these events. On August 31, 2006, the Costa Rican Attorney General's Office filed an amended complaint seeking compensation in the amount of $17.8 million for pecuniary damage caused generally to the Costa Rican people ("daño social"). Such amount is claimed on "provisional and prudential basis", and it may therefore be modified in the future. The amount of damages sought by the lawsuit filed by ICE has not yet been specified. Alcatel–Lucent intends to defend these actions vigorously and deny any liability or wrongdoing with respect to these litigations.

Alcatel–Lucent is unable to predict the outcome of these investigations and civil lawsuit and their effect on its business. If the Costa Rican authorities conclude criminal violations have occurred, CIT may be banned from participating in government procurement contracts within Costa Rica for a certain period and fines or penalties may be imposed on CIT, in an amount which Alcatel–Lucent is not able to determine at this time. Alcatel-Lucent expects to generate approximately €16 million in revenue from Costa Rican contracts in 2007. Based on the amount of revenue expected from these contracts, Alcatel–Lucent does not believe a loss of business in Costa Rica would have a material adverse effect on Alcatel–Lucent as whole. However, these events may have a negative impact on the image of Alcatel–Lucent in Latin America.

Taiwan

Certain employees of Taisel, a Taiwanese subsidiary of Alcatel–Lucent, and Siemens Taiwan, along with a few suppliers and a legislative aide, have been the subject of an investigation by the Taipei Investigator's Office of the Ministry of Justice relating to an axle counter supply contract awarded to Taisel by Taiwan Railways in 2003. It has been alleged that persons in Taisel, a German subsidiary of Alcatel–Lucent involved in the Taiwan Railway contract and Siemens Taiwan, and subcontractors hired by them were involved in a bid rigging and illicit payment arrangement for the Taiwan Railways contract.

Upon learning of these allegations, Alcatel commenced and is continuing an investigation into this matter. Alcatel terminated the former president of Taisel. A director of international sales and marketing development of the German subsidiary resigned.

On February 21, 2005, the former president of Taisel, Taisel and others were indicted in Taiwan for violation of the Taiwanese Government Procurement Act.

On November 15, 2005, the Taipei criminal district court found Taisel not guilty of the alleged violation of the Government Procurement Act. The former President of Taisel was not judged because he was not present or represented at the proceedings. The court found two Taiwanese businessmen involved in the matter guilty of violations of the Business Accounting Act.

The prosecutor has filed an appeal with the Taipei court of appeals. Should the higher court find Taisel guilty of the bid–rigging allegations in the indictment, Taisel may be banned from participating in government procurement contracts within Taiwan for a certain period and fines or penalties may be imposed on Alcatel, in an amount not to exceed €25,000.

Other allegations made in connection with this matter may still be under ongoing investigation by the Taiwanese authorities.

The SEC and the Department of Justice are also looking into these allegations in conjuction with their investigation relating to the allegations in Costa Rica.

As a group, Alcatel–Lucent expects to generate €148 million of revenue from Taiwanese contracts in 2007, of which only a part will be from governmental contracts. Based on the amount of revenue expected from these contracts, Alcatel–Lucent does not believe a loss of business in Taiwan would have a material adverse effect on Alcatel–Lucent as a whole.

Kenya

As part of their investigation regarding Costa Rica, the SEC and the Department of Justice have asked Alcatel–Lucent to look into payments made by CIT to a consultant arising out of a supply contract between CIT and a privately–owned company in Kenya. Alcatel–Lucent is cooperating with the U.S. authorities and is looking into those payments as requested.

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Former Lucent's Securities and Related Cases

On April 3, 2006, a putative class action entitled *Resnick v. Lucent Technologies Inc., et al* was filed against Lucent and members of Lucent's board of directors in the Superior Court of New Jersey, Law Division, Union County. The named plaintiffs proposed to represent a class of Lucent shareowners and claimed that, among other things, the proposed merger with Alcatel was the product of breaches of duty by Lucent's board of directors in that they allegedly failed to maximize shareowner value in the transaction. On May 12, 2006, a second putative class action entitled *AR Maley Trust v. Lucent Technologies Inc., et al* was filed against Lucent and members of Lucent's board of directors in the United States District Court for the Southern District of New York. The named plaintiff proposed to represent a class of Lucent's shareowners and claimed that, among other things, Lucent and the directors breached their fiduciary duties by allegedly failing to maximize shareowner value in the transaction. Along with other relief, both the *Resnick* and *AR Maley Trust* complaints sought an injunction against the closing of the proposed merger. On September 6, 2006, Lucent reached a tentative settlement of these actions. The settlement is subject to customary conditions including court approval. The settlement does not require any payment to class members but requires a payment of $250,000 for plaintiff's counsel. On February 26, 2007 the court approved the settlement of these actions.

Government Investigations related to Lucent

In August 2003, the U.S. Department of Justice (DOJ) and the SEC informed Lucent that they had each commenced an investigation into possible violations of the Foreign Corrupt Practices Act (FCPA) with respect to Lucent's operations in Saudi Arabia. These investigations followed allegations made by National Group for Communications and Computers Ltd. (NGC) in an action filed against Lucent on August 8, 2003, which is described below. In April 2004, Lucent reported to the DOJ and the SEC that an internal FCPA compliance audit and an outside counsel investigation found incidents and internal control deficiencies in Lucent's operations in China that potentially involve FCPA violations. Lucent is cooperating with those agencies. Lucent believes these incidents and deficiencies did not have a material effect on its results of operations. However, Lucent cannot determine whether this continuing investigation will affect its future business operations in China. The investigation is continuing with respect to both China and Saudi Arabia.

During September 2006, Lucent received a Wells notice relating to this investigation of its operations in China under the FCPA. Lucent responded to the Wells notice via a written submission to the SEC staff and is continuing discussions with the SEC staff in an effort to resolve the matter.

In May 2005, Lucent received subpoenas on two different matters, requesting specific documents and records. One of the subpoenas relates to a DOJ investigation of potential antitrust and other violations by various participants in connection with the United States government's E–Rate program. The subpoena requires Lucent to produce documents before a grand jury of the U.S. District Court in Georgia. The second subpoena was from the Office of Inspector General, U.S. General Services Administration and relates to a federal investigation into certain sales to the federal government of telecommunications equipment and related maintenance services. During April 2006, the California Department of Justice served Lucent with discovery requests related to sales to California governmental agencies of telecommunications equipment and related maintenance services. It is too early for Lucent to determine whether any of these matters will have a material effect on Lucent business, financial position, results of operations or cash flows.

Lucent's Employment and Benefits Related Cases

Lucent has implemented various actions to address the rising costs of providing retiree health care benefits and the funding of Lucent pension plans. These actions have led to the filing of cases against Lucent and may lead to the filing of additional cases. Purported class action lawsuits have been filed against Lucent in connection with the elimination of the death benefit from its U.S. management pension plan in early 2003. Three such cases have been consolidated into a single action pending in the U.S. District Court in New Jersey, captioned *In Re Lucent Death Benefits ERISA Litigation*. The elimination of this benefit reduced Lucent future pension obligations by approximately $400 million. The benefit was paid out of the pension plan assets to certain qualified surviving dependents, such as spouses or dependent children of management retirees. The case alleges that Lucent wrongfully terminated this death benefit and requests that it be reinstated, along with other remedies. This case has been dismissed by the court, but the dismissal has been appealed to a higher court and that appeal is pending. Another such case, *Chastain, et al. v. AT&T*, was filed in the U.S. District Court in the Western District of Oklahoma. The *Chastain* case also involves claims related to changes to retiree health care benefits.

In October 2005, a purported class action was filed by Peter A. Raetsch, Geraldine Raetsch and Curtis Shiflett, on behalf of themselves and all others similarly situated, in the U.S. District Court for the District of New Jersey. The plaintiffs in this case allege that Lucent failed to maintain health care benefits for retired management employees as required by the Internal Revenue Code, the Employee Retirement Income Security Act, and the Lucent pension and medical plans. Upon motion by Lucent, the court remanded the claims to Lucent's claims review process. A Special Committee was appointed and reviewed the claims of the plaintiffs and Lucent filed a report with the Court on December 28, 2006. The Special Committee denied the plaintiffs' claims and the case has returned to the court, where limited discovery is underway.

The Equal Employment Opportunity Commission (EEOC) filed a purported class action lawsuit against Lucent, *EEOC v. Lucent Technologies Inc.*, in the U.S. District Court in California. The case alleges gender discrimination in connection with the provision of service credit to a class of present and former Lucent employees who were out of work because of maternity prior to 1980 and seeks the restoration of lost service credit prior to April 29, 1979, together with retroactive pension payment adjustments, corrections of service records, back pay and recovery of other damages and attorneys fees and costs. The case is stayed pending the disposition of an appeal raising similar issues in another case before the applicable appellate court.

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Lucent's Intellectual Property Cases

Lucent is a defendant in various cases in which third parties claim infringement of their patents, including certain cases where infringement claims have been made against its customers in connection with products Lucent have provided to them.

Lucent's other litigations

Winstar

Lucent is a defendant in an adversary proceeding originally filed in U.S. Bankruptcy Court in Delaware by Winstar and Winstar Wireless, Inc. in connection with the bankruptcy of Winstar and various related entities. The trial for this matter concluded in June 2005. The trial pertained to breach of contract and other claims against Lucent, for which the trustee for Winstar was seeking compensatory damages of approximately $60 million, as well as costs and expenses associated with litigation. The trustee was also seeking recovery of a payment Winstar made to Lucent in December 2000 of approximately $190 million plus interest. On December 21, 2005, the judge rendered his decision and the verdict resulted in a judgment against Lucent for approximately $244 million, plus statutory interest and other costs. As a result, Lucent has recognized a $290 million charge (including related interest and other costs of approximately $46 million) as of December 31, 2006. In addition, $311 million of cash was used to collateralize a letter of credit that was issued during the second quarter of fiscal 2006 in connection with this matter. This judgment is under appeal with the U.S. District Court for the District of Delaware. Additional charges for post–judgment interest will be recognized in subsequent periods until this matter is resolved. Lucent is required to renew the letter of credit in April 2007, which may require recollateralization.

NGC

On August 8, 2003, NGC filed an action in the U.S. District Court for the Southern District of New York against Lucent, certain former officers and employees, Lucent subsidiary, Lucent Technologies International Inc., certain unaffiliated individuals and an unaffiliated company, alleging violations of the Racketeer Influenced Corrupt Organizations Act (RICO) and other improper activities. These allegations relate to activities in Saudi Arabia in connection with certain telecommunications contracts involving Lucent, the Kingdom of Saudi Arabia and other entities. The complaint seeks damages in excess of $63 million, which could be tripled under RICO. The allegations in this complaint appear to arise out of certain contractual disputes between NGC and Lucent that are the subject of a separate case that NGC previously filed against Lucent in U.S. District Court in New Jersey and other related proceedings brought by NGC in Saudi Arabia. On March 1, 2006, the District Court in New York granted Lucent motion to dismiss the case in its entirety. NGC has filed a notice of appeal. Some of the claims brought by NGC in the New Jersey action have been dismissed, but that case and the other claims in Saudi Arabia are still pending.

Effect of the various investigations and procedures

Alcatel–Lucent reiterates that its policy is to conduct its business with transparency, and in compliance with all laws and regulations, both locally and internationally. Alcatel–Lucent will cooperate with all governmental authorities in connection with the investigation of any violation of those laws and regulations.

Although it is not possible at this stage of these proceedings to predict the outcome with any degree of certainty, Alcatel–Lucent believes that the ultimate outcome of these proceedings will not have a material adverse effect on its consolidated financial position or its income (loss) from operating activities. Alcatel–Lucent is not aware of any other exceptional circumstances or proceedings that have had or may have a significant impact on the business, the financial position, the net income (loss) or the assets of Alcatel–Lucent or the Group.

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Note 35 – Events after the balance sheet date

At the Extraordinary General Shareholders Meeting of January 5, 2007, Thales shareholders approved the resolutions relative to the contribution of Alcatel–Lucent's transportation and security activities to Thales. This Meeting brings to a close the first phase of the agreement signed with Alcatel–Lucent in December 2006. A second phase, regarding the acquisition in cash of Alcatel–Lucent's space activities, should be finalized during the first half of 2007, subject to approval by the European Commission.

There were no other events, favorable or unfavorable, that occurred between the balance sheet date and February 8, 2007, the date when the Board of Directors authorized the consolidated financial statements for issue. However, the consolidated financial statements will only be final once approved by the Annual Shareholders' Meeting.

Note 36 –Main consolidated companies

Company	Country	% control	% interest	Consolidation method
Alcatel[2][3]	France			Parent company
OPERATING COMPANIES[1]				
Alcatel Australia Limited	Australia			Full consolidation
Alcatel Austria AG	Austria			Full consolidation
Alcatel Bell NV	Belgium			Full consolidation
Alcatel Business Systems S.A.	France			Full consolidation
Alcatel Canada Inc.	Canada			Full consolidation
Alcatel CIT	France			Full consolidation
Alcatel España S.A.	Spain			Full consolidation
Alcatel Indetel S.A. de CV	Mexico			Full consolidation
Alcatel Italia SpA	Italy			Full consolidation
Alcatel SEL AG	Germany			Full consolidation
Alcatel Shanghai Bell(c)	R.P.C.	50	50	Full consolidation
Alcatel Submarine Networks S.A.	France			Full consolidation
Alcatel Telecom Limited	U.K.			Full consolidation
Alcatel Telecom Nederland BV	The Netherlands			Full consolidation
Alcatel Telecommunicacoes SA	Brazil			Full consolidation
Alcatel USA Inc.	U.S.			Full consolidation
Alcatel Vacuum Technology France	France			Full consolidation
Alda Marine	France	51	51	Proportionate
Lucent Technologies Inc.	U.S.			Full consolidation
Lucent Technologies International Sales Ltd	Ireland			Full consolidation
Lucent Technologies Qingdao Telecom System Ltd	China	51	51	Full consolidation
Radio Frequency Systems GmbH	Germany			Full consolidation
Radio Frequency Systems Inc.	U.S.			Full consolidation

(1) Percentages of control and interest equal 100% unless otherwise specified.
(2) Publicly traded.
(3) Financial data for Alcatel-Lucent, as the parent company, are included in this business segment.

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Company	Country	% control	% interest	Consolidation method
HOLDINGS AND OTHER[3]				
Aerospace, defence and IT&S				
Thales (ex Thomson-CSF)[2]	France	12.8	9.5	Equity
Financial Holdings				
Alcatel NV	The Netherlands			Full consolidation
Alcatel Participations	France			Full consolidation
Compagnie Financière Alcatel	France			Full consolidation
Coralec	France			Full consolidation
Florelec	France			Full consolidation
Lucent Technologies International Inc.	U.S.			Full consolidation
Financial Services				
Electro Banque	France			Full consolidation
Electro Ré	Luxembourg			Full consolidation

(1) Percentages of control and interest equal 100% unless otherwise specified.
(2) Publicly traded.
(3) Financial data for Alcatel-Lucent, as the parent company, are included in this business segment.

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Note 37 – Quarterly information (unaudited)

Consolidated income statements

2006 *(in millions of euros)*	Q1	Q2	Q3	Q4	Total
Revenues	2,655	2,863	2,893	3,871	12,282
Cost of sales	(1,705)	(1,861)	(1,879)	(2,767)	(8,212)
Gross profit	**950**	**1,002**	**1,014**	**1,104**	**4,070**
Administrative and selling expenses	(458)	(459)	(461)	(532)	(1,910)
Research and development costs	(337)	(327)	(332)	(470)	(1,466)
Income (loss) from operating activities before restructuring costs, impairment of intangible assets and gain/(loss) on disposal of consolidated entities	**155**	**216**	**221**	**102**	**694**
Restructuring costs	(23)	(4)	(19)	(661)	(707)
Impairment of capitalized development costs	–	–	–	(141)	(141)
Gain/(loss) on disposal of consolidated shares	–	–	15	–	15
Income (loss) from operating activities	**132**	**212**	**217**	**(700)**	**(139)**
Financial interest on gross financial debt	(54)	(50)	(53)	(84)	(241)
Financial interest on cash and cash equivalents	33	27	32	51	143
Finance costs	(21)	(23)	(21)	(33)	(98)
Other financial income (loss)	(21)	7	(41)	(57)	(112)
Share in net income (losses) of equity affiliates	5	16	6	(5)	22
Income before tax and discontinued operations	**95**	**212**	**161**	**(795)**	**(327)**
Reduction of goodwill related to realized unrecognized tax loss carry forwards	–	–	–	(5)	(5)
Income tax expense	(12)	(40)	(8)	102	42
Income (loss) from continuing operations	**83**	**172**	**153**	**(698)**	**(290)**
Income (loss) from discontinued operations	30	28	16	85	159
NET INCOME (LOSS)	**113**	**200**	**169**	**(613)**	**(131)**
Attributable to:					
– Equity holders of the parent	**104**	**180**	**155**	**(615)**	**(176)**
– Minority interests	9	20	14	*2*	*45*
Net income (loss) attributable to the equity holders of the parent per share *(in euros)*					
– Basic earnings per share	0.08	0.13	0.11	(0.37)	(0.12)
– Diluted earnings per share	0.08	0.13	0.11	(0.37)	(0.12)
Net income (loss) of discontinued operations per share *(in euros)*					
– Basic earnings per share	0.06	0.11	0.10	(0.42)	(0.23)
– Diluted earnings per share	0.06	0.11	0.10	(0.42)	(0.23)
Net income (loss) of discontinued operations per share *(in euros)*					
– Basic earnings per share	0.02	0.02	0.01	0.05	0.11
– Diluted earnings per share	0.02	0.02	0.01	0.05	0.11